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FISCAL IMPACT STATEMENT

LS 7888

BILL NUMBER: SB 525

NOTE PREPARED: Jan 17, 2003

BILL AMENDED:

SUBJECT: Economic Development in Closed Military Bases.

FIRST AUTHOR: Sen. Weatherwax

FIRST SPONSOR:

BILL STATUS: As Introduced

FUNDS AFFECTED: ☒ **GENERAL**
☒ **DEDICATED**
FEDERAL

IMPACT: State

Summary of Legislation: The bill provides the following tax incentives to a business that locates new operations in certain qualified areas that contain a completely or partially inactive or closed military base: (1) A Sales Tax exemption for sales of utility services or commodities made to the business. (2) A Corporate Adjusted Gross Income (AGI) Tax rate of 5% for the year of relocation and the next succeeding four taxable years. The bill also provides a Military Base Investment Cost Credit against state tax liability for a taxpayer who purchases an ownership interest in or otherwise invests in a business located in a qualified area. The bill provides that the various tax incentives are not available to the extent that the business substantially reduces or ceases its operations at another location in Indiana in order to relocate them within the qualified area. The bill increases the Enterprise Zone Loan Interest Credit from 5% to 15% of the amount of interest received by the taxpayer. It also makes the Enterprise Zone Investment Cost Credit available to a taxpayer that makes an investment: (1) in a business that locates new operations in an Enterprise Zone; and (2) in which the taxpayer does not acquire an ownership interest in the business.

Effective Date: July 1, 2003; January 1, 2004.

Explanation of State Expenditures: The Department of State Revenue (DOR) would incur some administrative expenses relating to the revision of tax forms, instructions, and computer programs to incorporate the new tax incentives and tax credit changes under the bill. The DOR also would be required to make certain eligibility determinations relating to investment tax credits claimed for debt financing to businesses in Enterprise Zones and certain military base areas. The Indiana Department of Commerce (IDOC) also would incur administrative expenses relating to determining eligibility and credit amounts for these investment credits. These expenses presumably could be absorbed given the existing budget and resources of each agency.

Explanation of State Revenues: *Military Base Incentives:* The bill establishes three new tax incentives relating to businesses that locate new operations or expansions after June 30, 2003 within the boundaries of: (1) a military base that is scheduled for closing or closed; (2) a Military Base Reuse Area; (3) an Economic Development Area established in connection with a closed military base; and (4) a Military Base Recovery Site. According to the IDOC, there are currently three installations in Indiana that are both Enterprise Zones and Military Base Reuse Areas - Grissom AFB in Miami County, Fort Benjamin Harrison in Marion County, and the Indiana Army Ammunition Plant in Clark County.

The total amount that could potentially be claimed by businesses under the three tax incentives is indeterminable. The net revenue impact of these tax incentives depends on extent that collections on taxable activities attributable to new business locations or business expansion within the military base areas is less than or exceeds the tax incentives claimed. It also depends on the extent that collections relating to relocated operations in the military base areas are less than or exceed the taxes that would otherwise have been collected on these operations elsewhere in the state. However, if the business location or expansion would have occurred in the absence of the tax incentives, the net impact would be the total of the incentives claimed by businesses. It is important to note that the sales tax exemption for purchases of utility services would have no fiscal impact to the extent that utilities purchased by eligible businesses are for direct consumption as a material to be consumed in the direct production of other tangible personal property. These purchases would already be tax-exempt under current statute. The incentives for businesses locating within these areas are as follows.

(1) The bill provides a Sales Tax exemption for utility services purchased by a business that locates all or part of its operations in one of the above-described military base areas.

(2) The bill reduces the Adjusted Gross Income (AGI) Tax rate from 8.5% to 5% for a corporation that locates all or part of its operations to one of the above-described military base areas. The rate reduction applies only to income derived by the corporation from sources within Indiana during the taxable year in which operations were located or expanded in the area, and the next four succeeding taxable years.

(3) The bill establishes a non-refundable AGI Tax credit (the Military Base Investment Cost Credit) for investment a business that locates all or part of its operations to one of the above-described military base areas. Creditable investment would include both equity financing and debt financing. The bill allows the Indiana Department of Commerce (IDOC) to award credits for the cost of investment and for jobs created due to the investment. The percentage credits allowed vary depending upon the type of investment, the type of business, and the number of jobs created. (The credits are the same as those provided under the existing Enterprise Zone Investment Cost Credit.) The taxpayer may carry forward any unused credit amount to subsequent taxable years. The taxpayer is not eligible to carry back any unused credit. For pass through entities, the credit may be claimed by shareholders, partners, or members in proportion to their distributive income from the pass through entity.

Generally, the three new tax incentives do not apply to a business that substantially reduces or ceases operations at another location in Indiana. (Note: This condition does not apply to equity financing under the Military Base Investment Cost Credit.) However, the incentives apply if the Department of State Revenue (DOR) determines that the business had existing operations in the military base area and the relocated operations are an expansion of those existing operations. The sales tax exemption is effective for transactions occurring after June 30, 2003. The income tax incentives are effective beginning in tax year 2004. Contingent on project startups, the fiscal impact could potentially begin in FY 2004 - with monthly sales tax remittances and changes in estimated quarterly income tax payments.

Enterprise Zone Credits: The bill makes changes to two Adjusted Gross Income (AGI) Tax credits relating to loans and investment to Enterprise Zone (EZ) businesses. The bill increases the EZ Loan Interest Credit from 5% to 15% and extends the EZ Investment Cost Credit to debt financing (currently limited to equity investment). These two changes could lead to a significant increase in the total amounts claimed under these two credits. The bill triples the percentage credit for qualified EZ loan interest, but also extends the investment cost credit to debt financing. Thus, a creditor could potentially access a credit for the debt financing to an EZ business and for the interest on that same loan. Effectively, the net revenue impact of the tax credit changes depend on the extent that collections on taxable activities attributable to the creditable investment or improvements within the EZs is less than or exceeds the tax credits claimed. However, if the investment or improvements would have occurred in the absence of the increased tax credits, the net impact would be the total of the additional credits claimed by taxpayers. The changes to both EZ tax credits are effective beginning in tax year 2004. Contingent on project startups, the fiscal impact could potentially begin in FY 2004 - with changes in estimated quarterly income tax payments.

The tax credit changes also could potentially increase registration fee revenue to the state Enterprise Zone Board. Businesses with a tax savings exceeding \$1,000 during the year must pay the EZ Board a registration fee equal to 1% of the tax savings. Additional investment and employment resulting from the tax credit changes also could potentially increase taxpayer claims for the EZ Employment Expense Credit and the EZ Employee Tax Deduction to the extent that additional employees reside within the EZ.

Under current statute, the EZ Loan Interest Credit is equal to 5% of the interest a taxpayer receives on loans to EZ businesses that are used for: (1) a purpose that is directly related to an EZ business; (2) an improvement that increases the assessed value of real property located in an EZ; or (3) rehabilitation, repair, or improvement of a residence. In addition, current statute limits the EZ Investment Cost Credit to equity financing provided to EZ businesses. However, the credit for debt financing added by this bill does not apply to a business that substantially reduces or ceases operations at another location in Indiana. (Note: This condition does not apply to equity financing.) However, the credit applies if the Department of State Revenue (DOR) determines that the business had existing operations in the EZ and the relocated operations are an expansion of those existing operations.

Tax Distributions: Revenue from the AGI Tax on corporations is distributed to the state General Fund. Eighty-six percent of the revenue from the AGI Tax on individuals is deposited in the state General Fund, and 14% of this revenue is deposited in the Property Tax Replacement Fund. Sales Tax revenue is deposited in the Property Tax Replacement Fund (50%), the state General Fund (49.192%), the Public Mass Transportation Fund (0.635%), the Commuter Rail Service Fund (0.14%), and the Industrial Rail Service Loan Fund (0.033%).

Explanation of Local Expenditures:

Explanation of Local Revenues: The changes to EZ tax credits could potentially affect local option income taxes in local units with EZs. The extent of this impact is indeterminable and contingent on the new investment and employment that occurs as a result of the bill. Also, any local option income tax impact would rely on new employees that are not eligible for the existing EZ Employee Tax Deduction. Also, new development resulting from the tax credit changes would be placed on the property tax rolls. This could help spread the property tax burden and could possibly reduce some tax rates.

State Agencies Affected: Indiana Department of Commerce; State Department of Revenue; Enterprise Zone Board.

Local Agencies Affected: Local units with Enterprise Zones and closed military bases.

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